



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL ON MADIBENG LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of Madibeng Local Municipality, which comprise the statement of financial position as at 30 June 2009, and the statement of financial performance, statement of changes in net assets and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information, as set out on pages [XX] to [XX].

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act of South Africa, 2008 (Act No. 2 of 2008) (DoRA) and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. As required by section 188 of the Constitution of Republic of South Africa, 1996 (Act No. 108 of 1996) and section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) my responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with the International Standards on Auditing and *General Notice 1111 of 2010* issued in *Government Gazette 33872 of 15 December 2010*. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Corresponding figures

4. All the matters giving rise to the prior year's qualifications remain unresolved, thus I was unable to determine the completeness, existence, valuation and allocation, rights and obligations and presentation and disclosure of the corresponding figures for net assets of R835 709 489, non-current liabilities of R91 088 522, current liabilities of R574 289 847, non-current assets of R1 368 339 335 and current assets of R132 748 523 disclosed in the statement of financial position. The municipality did not meet the disclosure requirements of SA Standards of GRAP, GRAP 3, *Accounting Policies, Changes in Accounting Estimates and Errors*, paragraphs 41 to 49, in instances where prior year balances were restated.

Property, plant and equipment

5. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, existence and rights and obligations of property, plant and equipment of R1 386 951 833 disclosed in note 8 to the financial statements. Alternative procedures indicated completed

capital projects of R22 600 604 which should have been capitalised, a lack of detail as required by SA Standards of GRAP, GRAP17, *Property, plant and equipment* paragraph 53 to depreciate each item separately and a lack of review of residual values. The municipality's system and records did not permit the performance of further alternative audit procedures.

Long-term receivables

6. SA Standards of GRAP, IAS 39, *Financial Instruments: Recognition and Measurement* requires an assessment of the impairment of debtors. Housing debtors who did not make any payments in terms of their contractual agreement is indicative that these debtors might be impaired. No provision under these circumstances were made, therefore long-term debtors are overstated. The municipality's system did not permit the application of alternative audit procedures and I could not practicably determine the resulting misstatement in long term receivables. I was also unable to obtain sufficient appropriate audit evidence to re-perform the calculation of the short-term portion of long-term debtors. Consequently, I was unable to determine the completeness, existence, valuation and allocation, rights and obligations of long-term receivables of R12 457 849 disclosed in note 10 to the financial statements

Consumer debtors

7. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, existence, valuation and allocation and rights and obligations of consumer debtors of R124 498 578 disclosed in note 12 to the financial statements. The municipality's records did not permit the application of alternative audit procedures.

Bank overdraft

8. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, valuation and allocation of the bank overdraft of R36 328 495 disclosed in the statement of financial position. Alternative procedures indicated cheques of R29 419 626 printed before year-end but not issued. These invalid outstanding cheques are incorrectly included in the bank overdraft, resulting in creditors being understated and the bank overdraft overstated by this amount. The municipality's records did not permit the application of further audit procedures and further misstatements could not be practicably quantified.

Accumulated surplus and reserves

9. I was unable to obtain sufficient appropriate audit evidence for reserves of R291 449 797, unbundling adjustments of R1 132 013 194 and prior year adjustments of R266 224 395 included in the accumulated surplus of R23 061 756 in the statement of changes in net assets and statement of financial position. The municipality's system did not permit the application of alternative audit procedures. Consequently, I could not determine the existence, completeness, valuation and allocation, rights and obligations of the accumulated surplus.
10. I was unable to obtain sufficient appropriate audit evidence for the capitalisation reserve of R222 224 166 disclosed in the statement of changes in net assets and the statement of financial position. The municipality's system did permit the application of alternative audit procedures. Consequently, I could not determine the existence, completeness, valuation and allocation, rights and obligations of the capitalisation reserve.
11. I was unable to obtain sufficient appropriate audit evidence for the government grant reserve of R588 784 414 disclosed in the statement of changes in net assets and the statement of financial position. The municipality's system did not permit the application of alternative audit procedures. Consequently, I could not determine the existence, completeness, valuation and allocation, rights and obligations of the government grant reserve.

Provisions

12. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, existence, valuation and allocation and the rights and obligations of provisions of R59 068 893 disclosed in the statement of financial position. The municipality's system did not permit the application of alternative audit procedures.

Creditors

13. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, existence, valuation and allocation and rights and obligations of creditors of R187 081 534 disclosed in note 6 to the financial statements. The municipality's records did not permit the application of alternative audit procedures.

Value-added tax (VAT)

14. I was unable to determine the completeness, valuation and allocation of the VAT liability of R24 575 626 due to the municipality's inability to provide sufficient appropriate audit evidence to explain the difference of R5 193 908 between the VAT 201 returns and the amount disclosed in note 7 to the financial statements.

Revenue

15. I was unable to obtain sufficient appropriate audit evidence for grants and subsidies of R288 903 884, property rates of R107 770 634, service charges of R237 847 975 and other income of R10 932 897 disclosed in the statement of financial performance. The municipality's system did not permit the application of alternative audit procedures. Consequently, I could not determine the occurrence, completeness, accuracy and classification of this revenue.

Expenditure

16. I was unable to obtain sufficient appropriate audit evidence for repairs and maintenance of R33 138 391, contracted services of R67 696 487, general expenses of R98 696 426 and depreciation expenditure of R38 661 639 disclosed as operating expenditure in the statement of financial performance. The municipality's records did not permit the application of alternative procedures. Consequently, I could not determine the occurrence, accuracy, classification, cut-off and completeness and this expenditure.
17. I was unable to obtain sufficient appropriate audit evidence for journals of R155 570 547 processed during the year. These journals were processed across all account balances. The municipality's records did not permit the application of alternative procedures regarding these journals. I was unable to determine the effect of this limitation on the other account balances or classes of transactions contained in the financial statements.

Contingent liabilities

18. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, valuation and allocation of contingent liabilities of R25 083 088 disclosed in note 33 to the financial statements. Alternative procedures indicated a claim of R6 000 000 against a supplier, which was incorrectly classified as a contingent liability resulting in the overstatement of contingent liabilities. The municipality's system did not permit the application of further audit procedures therefore the resulting misstatement in contingent liabilities could not practicably determined.

Commitments

19. I was unable to obtain sufficient appropriate audit evidence to determine the completeness, existence, valuation and allocation, rights and obligations of approved and contracted for and

approved not yet contracted for commitments of R221 878 779 and R114 970 297 respectively included in commitments of R336 849 076 as per note 31 to the financial statements.. The municipality's records did not permit the application of alternative procedures.

Unauthorised expenditure

20. The municipality exceeded its approved expenditure budget with R135 344 511. The municipality however only disclosed unauthorised expenditure of R64 589 228 in note 29 to the financial statements as resulting in unauthorised expenditure being understated by R70 755 283.

Irregular expenditure

21. Section 125(d)(i) of the MFMA requires the municipality to include in the notes to the financial statements particulars of any material irregular expenditure incurred during the year. Contrary to this requirement no irregular expenditure was disclosed in the notes to the financial statements and I was unable to obtain sufficient appropriate audit evidence to determine the extent of irregular expenditure. Alternative procedures indicated the existence of irregular expenditure of R17 428 377 due to non compliance with supply chain management regulations. The municipality's system did not permit the performance of further alternative audit procedures. Consequently, I was unable to satisfy myself as to the completeness of irregular expenditure and the misstatement could not be practicably determined.

Fruitless and wasteful expenditure

22. Section 125(d)(i) of the MFMA requires the municipality to include in the notes to the financial statements particulars of any fruitless and wasteful expenditure incurred during the year. Contrary to this requirement no fruitless and wasteful expenditure was disclosed in the notes to the financial statements and I was unable to obtain sufficient appropriate audit evidence to determine the extent of fruitless and wasteful expenditure. Alternative procedures indicated the existence of fruitless and wasteful expenditure due to payment of penalties and interest and payments made to consultants for poor quality services. The municipality's system did not permit the performance of further alternative audit procedures. Consequently, I was unable to satisfy myself as to the completeness of fruitless and wasteful expenditure and the misstatement could not be practicably determined.

Related parties

23. SA Standards of GRAP, IPSAS 20, *Related Party Disclosures* requires the disclosure of the nature of related party relationships. Contrary to these requirements, the types of transactions and the elements of the transactions necessary to clarify the significance of these transactions to its operations, sufficient to enable the financial statements to provide relevant and reliable information for decision-making and accountability purposes, were not disclosed in the notes to the financial statements.

Disclaimer of opinion

24. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on these financial statements.

Emphasis of matter

25. I draw attention to the matters below. My opinion is not modified in respect of the matter:



Going concern

26. The accounting officer reported in note 3 to the financial statements that the municipality currently owes R395 339 993 to the Public Investment Corporation. As this liability forms part of the current liabilities it is indicative that there is material uncertainty that cast significant doubt on the entity's ability to continue as a going concern.

Unauthorised expenditure

27. As disclosed in note 29 to the financial statements, unauthorised expenditure of R64 589 228 in respect of prior years had not been dealt with in accordance with section 32 of the MFMA.

Additional matter

28. I draw attention to the matter below. My opinion is not modified in respect of this matter:

Unaudited supplementary schedules

29. The supplementary information set out on pages [xx] to [xx] does not form part of the financial statements and is presented as additional information. I have not audited these schedules and accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

30. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages [XX] to [XX] and material non-compliance with laws and regulations applicable to the municipality.

Predetermined objectives

Usefulness of information

31. The reported performance information was deficient in respect of the following criteria:
- Consistency: The reported objectives, indicators and targets are consistent with the approved strategic plan and integrated development plan.
 - Relevance: There is a clear and logical link between the objectives, outcomes, outputs, indicators and performance targets.
 - Measurability: The indicators are well defined and verifiable, and targets are specific, measurable, and time bound.

The following audit findings relate to the above criteria:

Reported objectives are not consistent when compared with the planned objectives

32. Reported performance against predetermined objectives is not consistent with the approved integrated development plan.

Reliability of information

33. The reported performance information was deficient in respect of the following criteria:
- Validity: The reported performance did not occur and does not pertain to the entity.
 - Accuracy: The amounts, numbers and other data relating to reported actual performance have not been recorded and reported appropriately.
 - Completeness: All actual results and events that should have been recorded have not been included in the reported performance information.



The following audit findings relate to the above criteria:

Sufficient appropriate evidence was not submitted to support reported indicators and targets

34. Sufficient appropriate evidence in relation to any of the selected objectives could not be obtained. There were no satisfactory audit procedures that I could perform to obtain the required assurance as to the validity, accuracy and completeness of the reported performance against predetermined objectives.

Compliance with laws and regulations

Strategic planning and performance management

35. The municipality did not implement a framework that describes and represents how the municipality's cycle and processes of performance planning, monitoring, measurement, review, reporting and improvement will be conducted, organised and managed, including determining the roles of the different role players as required by sections 38, 39, 40 and 41 of the Municipal Systems Act (MSA) and Municipal Planning and Performance Management Regulations 7 and 8.

Budgets

36. The municipality incurred expenditure in excess of the limits of the amounts provided for in the votes in the approved budget, in contravention of section 15 of the MFMA.

Annual financial statements, performance and annual reports

37. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements identified by the auditors were not adequately corrected, which resulted in the financial statements receiving a disclaimer of audit opinion.
38. The accounting officer did not submit the annual financial statements of the municipality for auditing, within two months after the end of the financial year as required by section 126(1)(a) of the MFMA.

Procurement and contract management

39. Goods and services with a transaction value of between R10 000 and R200 000 were procured without obtaining written price quotations from at least three different prospective providers as per the requirements of SCM regulation 17(a) & (c).
40. A list of accredited prospective providers was not in place for procuring goods and services through quotations as required by SCM regulation 14(1)(a).

Expenditure

41. Money owing by the municipality was not always paid within 30 days of receiving an invoice or statement, as required by section 65(2)(e) of the MFMA.
42. The accounting officer did not take reasonable steps to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Revenue management

- 43. The council did not adopt and implement a tariff policy on the levying of fees for municipal services provided by the municipality, contrary to section 74(1) of the MSA.
- 44. A credit control and debt collection policy was not implemented as required by section 96(b) of the MSA.
- 45. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounted for debtors, as required by section 64(2)(e) of the MFMA.

Asset management

- 46. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounts for the assets of the municipality as required by section 63(2)(a) of the MFMA.

Financial misconduct

- 47. Disciplinary or criminal proceedings were not instituted against officials of the municipality, when investigations warranted such a step, as required by section 171 or 173 of the MFMA.

INTERNAL CONTROL

- 48. In accordance with the PAA and in terms of *General Notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

- 49. Sound integrity and ethical values to promote a culture of honesty, with ethical business practices and good governance, protecting and enhancing the best interests of the entity is not understood or implemented in order to set the standard of conduct for financial and performance reporting, and to ensure compliance with legislation.
- 50. Adequate oversight responsibility regarding financial and performance reporting and compliance and related internal controls are not exercised.
- 51. Effective HR management is not implemented, to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored. Personnel are not aware of the allocation of duties, responsibilities and lines of reporting. Key officials are not available throughout the audit process. An effective organisational structure that places people with appropriate skills is not established.
- 52. Actions are not taken to address risks relating to the achievement of complete and accurate financial and performance reporting and internal and external audit findings are not addressed.

Financial and performance management

- 53. Adequate controls over daily and monthly processing and reconciling of transactions do not exist. In addition controls are not designed to prevent and detect unauthorised, fruitless and wasteful and irregular expenditure. Furthermore, manual or automated controls are not designed to ensure that the transactions occurred, are authorised, and are completely and accurately processed.
- 54. Accurate and complete financial and performance reports that are supported and evidenced by reliable information is not prepared. Numerous errors were noted in the annual financial

statements submitted for auditing, which indicates that the financial statements were not adequately reviewed by management before submitting the final version for auditing.

55. Management failed to design and implement formal controls to review and monitor compliance with applicable laws and regulations.

Governance

56. Management failed to implement appropriate risk management activities to ensure that regular risk assessments are conducted and that a risk strategy is developed and monitored to address the risks.

Rustenburg

30 November 2011



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